COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

Petition of NSTAR Electric for Approval of Revised Tariffs M.D.T.E. Nos. 100A, 101A, 200A, 201A, 300A and 301A Relating to the Terms and Conditions for Distribution Services and Competitive Suppliers	)	**D.T.E. 05-84**

COMMENTS OF THE

MASSACHUSETTS DIVISION OF ENERGY RESOURCES

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I. INTRODUCTION

On November 21, 2005, Boston Edison Company, Cambridge Electric Light Company and Commonwealth Electric Company, d/b/a NSTAR Electric (together, "NSTAR" or the "Company"), filed with the Department of Telecommunications and Energy (the "Department"), proposed revised tariffs M.D.T.E. Nos. 100A, 101A, 200A, 201A, 300A and 301A, with an effective date of January 1, 2006. The proposed tariff revisions relate to NSTAR's terms and conditions for distribution services and competitive suppliers.

According to the Company, the proposed tariff revisions are designed to address load volatility relating to the practice of certain retail competitive suppliers switching large commercial and industrial ("C & I") customers on and off basic/default service multiple times within a short period of time. The company contends that this practice has resulted in increased basic/default service prices for those customers that are unable to take advantage of multiple switching. The proposed tariff revisions prohibit customers taking basic/default service from returning to the same retail competitive suppler that previously served them for a period of six months from the effective date of the change from competitive generation services to basic/default service.

The Company has requested that the Department review the revised tariffs on or before January 11, 2006, in order to implement the changes for its next scheduled basic/default service procurement for large C & I customers. The Department has suspended the tariffs for further investigation until February 1, 2006.

II. DOER'S COMMENTS

The Department should reject the proposed changes to NSTAR's terms and conditions. NSTAR has not demonstrated that high electricity prices are caused by load volatility. Furthermore, even if customer switching was the root cause of higher prices, NSTAR has not demonstrated that its proposed changes will solve this problem. Rather, NSTAR's solution may cause other detrimental effects.

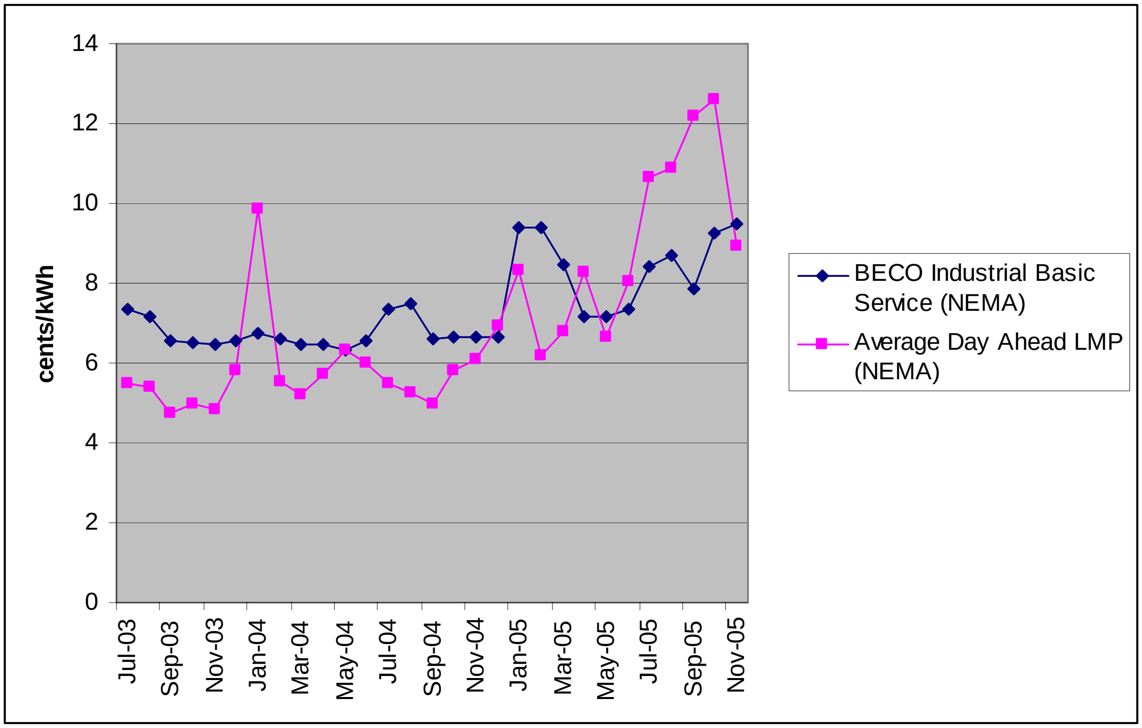
A. NSTAR Has Not Demonstrated That High Electricity Prices Are Caused By Load Volatility.

Though NSTAR spends considerable time describing the relationships among volatility, price, and switching practices of retail competitive suppliers, there is actually no measurement or quantification of the impact of load volatility on prices. NSTAR does not mention the possibility that other factors may have a much stronger causal affect on basic service prices than load volatility. Notably, there is no discussion of high and volatile wholesale spot prices (and the underlying volatile natural gas prices), the pricing premiums that may be introduced due to uncertainty in uplift, reliability-must-run (RMR) and procurement of other wholesale-related services and products, and any pricing premiums that may result from exertion of market power among wholesale electricity suppliers. Thus, in terms of percentage of an alleged premium, we cannot tell how much of the problems associated with high electricity prices the NSTAR approach seeks to resolve. Though we agree that recent high electric prices are problematic for Massachusetts ratepayers, NSTAR has failed to demonstrate that load switching is the leading cause.

Figure 1 below plots default/basic service prices against the average Northeastern Massachusetts (NEMA) on-peak, day-ahead locational marginal prices (LMPs) for the month, which can be considered a monthly spot wholesale market price. The graph shows that the basic service prices in NEMA are neither much higher nor much lower than the wholesale spot price for a majority of months. Indeed, taking simple averages of both sets of prices shows that over the time period July 2003--November 2005[1] (the last month for which wholesale prices are available) results in a 5 percent premium over wholesale prices. As expected, a 3-month price tends to be slightly less volatile than a monthly price, but the average price paid over the entire time period is close. The premium could be due to a number of factors, such as procurement of ancillary and capacity services, costs of congestion and RMR contracts, and load switching. The important questions that NSTAR has failed to answer is (a) how much of the 5 percent premium over wholesale price is due to load switching by customers and (b) how much of the premium the NSTAR approach will remove.

[1] DOER acknowledges that NSTAR's most recent basic service procurement resulted in prices that are extremely high—close to 20 cents/kWh. DOER believes that most if not all of these price hikes can be attributed to wholesale market developments, notably the anticipation of gas/electric shortages this winter, which have pushed up both gas and electric prices.

Figure 1 – Basic Service and Wholesale Spot Prices, July 2003 to November 2005



B. Even If Customer Switching Was The Root Cause Of Higher Prices, NSTAR Has Not Demonstrated That Its Proposed Changes Will Solve This Problem.

NSTAR's proposal does not eliminate load switching, per se. Customers will still be able to return to basic service and jump off basic service to another supplier. If this occurs, NSTAR's solution does nothing. Thus, it appears that NSTAR really does not have a problem with load-switching, rather NSTAR has a problem with load switching back to the same supplier. The only real solution to the load switching problem, as NSTAR has defined it, is to keep customers on basic service. Such an outcome would be antithetical to the goals of restructuring by imposing a restraint on the market that is not warranted by the evidence.

C. <u>NSTAR's Proposed Solution May Cause More Problems Than It Solves.</u>

Besides not resolving the problem at hand, the NSTAR approach may have negative impacts on customers. First, by its very nature, the NSTAR proposal seeks to influence long-term business relationships among customers and their competitive suppliers by prohibiting customers from returning to their existing supplier. Second, the NSTAR proposal removes an important option for suppliers by disallowing movement of customers to basic service. Presumably, such an option allows these competitive suppliers to provide more competitive and lower prices to their customers. Removing this option may have the impact of increasing prices to customers who are currently taking competitive supply. Whether this price increase offsets the anticipated price decrease from NSTAR's action is difficult to determine, but there could be movement away from competitive supply back to basic service. Finally, NSTAR's proposal may motivate shorter-term contracts or cause competitive suppliers to add additional premiums to longer term contracts. In turn, shorter term contracts at retail can translate to shorter-term contracts at the wholesale level, which has been mentioned as a major impediment to financing new generation.

D. <u>NSTAR Should Implement Hourly Pricing For Its Industrial Customers.</u>

If load switching is truly the problem NSTAR is trying to resolve, there are basically only two options (or hybrids of these two)—requiring customers to stay on basic service for a time period after they have switched from competitive supply or implementing hourly pricing, based on ISO's LMPs, for basic service. DOER supports the latter approach for a variety of reasons. First, the industrial customer class has been the most active participant in competitive markets. The percentage of load on competitive supply for this customer class for some months has been as high as 80 percent. These customers have the technical and financial ability to shop for power. Though it is true that there may be customers in this class that do not have favorable-enough load factors or credit to obtain competitive offers, it was not the intention of restructuring to provide competitive service to all customers, but to provide the option for customers to seek competitive offers. In well functioning markets for any product, prices should be higher for customers with lower credit or with demands that are difficult to serve.

Second, as shown by Figure 1, spot wholesale prices are not much greater than prices obtained through basic service provision, though they are more volatile. DOER believes that the intention behind a 3-month procurement (instead of a 6-month product as found for residential and small commercial and industrial customers), was to introduce some volatility to this customer class because of their ability to manage their loads and seek offers from the competitive market. Finally, hourly pricing supports other worthwhile policy objectives, such as advancement of demand response and better alignment with wholesale-market price signals.

III. CONCLUSION

In sum, DOER urges the Department to reject the NSTAR filing on the ground that it is premised on facts not substantiated in the record. It is based on anecdotal observations and speculation as to the potential cause and effect relationship. We believe that this poses a serious danger to the success of the competitive market to date for this class of customers. Further, the proposed remedy for the alleged problem smacks of a restraint of trade and is anticompetitive.

More importantly, to the extent the Department is persuaded that the problem posed by NSTAR in fact exists and causes the detrimental effects identified, DOER believes that this submittal presents the Department with an opportunity to move forward aggressively on devising a more appropriate and effective solution. That solution is the implementation of Real-Time Pricing (RTP) for large customers. Other jurisdictions have moved in this direction and ordered mandatory RTP for large customers (*See*, NYPUC Case 03-E-0641 Proceeding on Motion of the Commission Regarding Expedited Implementation of Mandatory Hourly Pricing for Commodity Service; *See also*, NJBPU Docket No. EO05040317, In the Matter of the Provision of Basic Generation Service for the Period Beginning June 1, 2006). This approach would eliminate the notice customers and competitive suppliers currently have as to the effective basic service rate or "price to beat" which precipitates the switching. Further, it has the added benefit of sending the right price signal to customers and, thereby, providing support for demand response programs and giving customers the opportunity to better control their electricity usage and costs.

The latter rationale has been the basis of much discussion in New England in the face of the current high prices across sectors. Further, the recently enacted Federal Energy Policy Act of 2005, directs states to conduct an investigation and issue a decision on whether or not it is appropriate for their state to move to time-based pricing and other demand response programs. See, Subtitle E: Amendments to PURPA, Section 1252. The question posed by NStar's filing is timely in the sense that it shows the need for the Department to move quickly forward on their investigation in the context of real market activity. At a time when momentum appears to be building to implement RTP for a myriad of other worthy policy reasons, it makes no sense to impose a rule change that will hamper rather than enhance the control large customers have over their electricity bills. We urge the Department to not be side tracked by a short-sighted and potentially harmful solution to broader pricing issues and seize the moment to show leadership toward a more effective and real solution.

Respectfully submitted,

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